

An Illinois retailer is one who either accepts purchase orders in the State of Illinois or maintains an inventory in Illinois and fills Illinois orders from that inventory. The Illinois retailer is liable for Retailers' Occupation Tax on gross receipts from sales and must collect the corresponding Use Tax incurred by purchasers. (This is a GIL).

May 25, 1999

Dear Xxxxx:

This letter is in response to your letter dated May 4, 1999. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

Good morning. COMPANY requests determination of nexus with the state of Illinois for the purpose of collecting and paying sales and use tax, franchise and income taxes and any other taxes for which we would be responsible. Following is an overview of our company structure, business activities and duties of the employee we have resident in the State.

COMPANY, incorporated in the STATE March 19,1999. We are an Internet based company in the business of selling books and software via the Internet, representing several small presses and a software developer as marketing representatives; and developing software packages to market to small publishers. We have no brick and mortar storefronts, leased or owned office space, inventory or other property in the state of Illinois or any other state. The four principals of the Company live in four different states and telecommute from their homes to work via the Internet.

Our employee in the State of Illinois is our webmaster and software developer. His duties are to maintain our website, ####, and develop software for internal use and to be marketed to the public. He has no specific or general duties which require him to be in the State, makes no sales contacts on behalf of the Company or does any work within the State that in any way enhances sales to Illinois residents. He is not located in the State for the convenience of the Company and is not required to live or work within the State. No employee of COMPANY is required to live in any specific geographic area. Our only residence requirement for all our employees is that they live where they will have reliable access to the Internet.

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A recent telephone conversation with an employee of the Department of Revenue revealed that the IDOR does consider us to have nexus based upon the residency of our employee, who works from his home. Our employees appear to meet the specific tests of 'substantial nexus' established by judicial precedent and prior interpretations of the Commerce Clause of the United States Constitution, specifically *Quill v. North Dakota*, 112 S.Ct. 1904 and the earlier decision upon which it was based, *Standard Steel Co. v. Washington Revenue Dept.* 419 U.S. 560. However, we feel that since our company is Internet based and these precedents and interpretations did not address or take Internet 'telecommuting' into consideration they should not apply. In those decisions, the physical presence of the employees directly benefited the companies in conducting business within the states. This reason for physical presence does not exist within our Company.

The Internet Tax Freedom Act (P.L. 105-277) does uphold the 'bright-line' physical presence test established by the above cases. However, Sec. 1101(a) states:

a) Moratorium. No State or political subdivision thereof shall impose any of the following taxes during the period beginning on October 1, 1998, and ending 3 years after the date of the enactment of this Act--

(1) taxes on Internet access, unless such tax was generally imposed and actually enforced prior to October 1, 1998; and

(2) multiple or discriminatory taxes on electronic commerce.

Additionally, Sec. 1104(2) sets the following definitions of discriminatory taxes:

(2) Discriminatory tax.--The term 'discriminatory tax' means--

(A) any tax imposed by a State or political subdivision thereof on electronic commerce that--

(i) is not generally imposed and legally collectible by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means;

(ii) is not generally imposed and legally collectible at the same rate by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished

through other means, unless the rate is lower as part of a phase-out of the tax over not more than a 5-year period;

(iii) imposes an obligation to collect or pay the tax on a different person or entity than in the case of transactions involving similar property, goods, services, or other information accomplished through other means;...(remainder omitted)

NOTE: The full text of The Internet Tax Freedom Act is available on the Internet at: #####.

Were it not for the ability of our employees to telecommute to work via the Internet we could not have an employee in Illinois and therefore could not conduct business in your state through other means.

For this reason we believe taxing an Internet based company whose employees telecommute to work via the Internet, whose employees are not located within the state specifically for the purpose of conducting work for the Company or for the convenience of the Company and could not live and work in the State were the Internet not available, is discriminatory in nature and prohibited by the Internet Tax Freedom Act.

Until such time as we receive a letter of nexus determination from IDOR on this request we will collect sales tax on any sales we may have to Illinois residents and maintain proper accounting records for payment of income and franchise taxes but it is to be understood they are being collected and remitted under protest.

We ask that you make a decision on this matter as expeditiously as possible. Thank you.

The Sales and Excise Tax Division of the Legal Services Office has received your letter. However, a copy has also been submitted to the Income Tax Division for a response. Please note that with regard to franchise taxes, the Office of the Secretary of State is responsible for charging and collecting such taxes. See the Business Corporation Act of 1983, 805 ILCS 5/1.01 *et seq.*

Illinois taxes the retail sale and use of tangible personal property under two separate but related statutes. The Retailers' Occupation Tax Act imposes a tax upon persons engaged in the business of selling at retail tangible personal property. 35 ILCS 120/2 (1996 State Bar Edition). The Use Tax Act imposes a tax upon the privilege of using in this State tangible personal property purchased at retail from a retailer. 35 ILCS 105/3 (1996 State Bar Edition). Intangibles are not subject to Retailers' Occupation Tax and Use Tax.

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The definition of a "retailer maintaining a place of business in Illinois" is set forth at 86 Ill. Adm. Code 150.201(i), see enclosed. An out-of-State retailer maintaining a place of business in this State is required to register with the State as an Illinois Use Tax collector. See the enclosed copy of 86 Ill. Adm. Code 150.801. The retailer must collect and remit Use Tax to the State on behalf of its Illinois customers even though the retailer does not incur any Retailers' Occupation Tax liability.

The final type of retailer is simply the out-of-State retailer that does not have sufficient nexus with Illinois to be required to submit to Illinois tax law. A retailer in this situation does not incur Retailer' Occupation Tax on sales into Illinois and is not required to collect Use Tax on behalf of its Illinois customers. However, the retailer's Illinois customers will still incur Use Tax on the purchase of the out-of-State goods and have a duty to self-assess their Use Tax liability and remit the amount directly to the State.

The United States Supreme Court in *Quill Corp. v. North Dakota*, 112 S.Ct. 1904 (1992), set forth the current guidelines for determining what nexus requirements must be met before a person is properly subject to a state's sales tax laws. The Supreme Court has set out a two-prong test for nexus. The first prong is whether the Due Process Clause is satisfied. Due Process will be satisfied if the person or entity purposely avails himself or itself of the benefits of an economic market in a forum state. *Id.* at 1910. The second prong of the Supreme Court's nexus test requires that, if due process requirements have been satisfied, the person or entity must have physical presence in the forum state to satisfy the Commerce Clause.

A physical presence does not mean simply an office or other physical building. Under Illinois tax law, it also includes the presence of any representative or other agent of the seller. The representative need not be a sales representative and it is immaterial for tax purposes that the representative's presence is temporary.

Sales of "canned" computer software are taxable retail sales in Illinois. See the enclosed copy of 86 Ill. Adm. Code 130.1935. If the computer software consists of custom computer programs, then the sales of such software are not taxable retail sales. See subsection (c) of Section 130.1935.

We do wish to emphasize that while there are no sales tax laws that specifically impose a tax on electronic commerce transactions, electronic commerce transactions may be subject to Illinois sales tax. There is nothing that exempts electronic commerce transactions from Illinois sales tax where applicable. This could include retail sales of any kind of tangible personal

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property, including sales of canned software, conducted via the Internet, wherein the vendor has nexus.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at [www.revenue.state.il.us](http://www.revenue.state.il.us). If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Gina Roccaforte  
Associate Counsel

GR:msk

Enc.